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This is the author version published as:

Christensen, Sharon A. and Duncan, William D. and Stickley, Amanda P.
(2009) *Behavioural biases and information disclosure laws relating to residential property sales : narrowing the gap between existing laws and calls for future reforms.* Queensland University of Technology Law and Justice Journal, 9(2). pp. 251-279.

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BEHAVIOURAL BIASES AND INFORMATION DISCLOSURE LAWS RELATING TO RESIDENTIAL PROPERTY SALES: NARROWING THE GAP BETWEEN EXISTING LAWS AND CALLS FOR FUTURE REFORMS¹

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Market failures involving the sale of complex merchandise, such as residential property, financial products and credit, have principally been attributed to information asymmetries. Existing legislative and regulatory responses were developed having regard to consumer protection policies based on traditional economic theories that focus on the notion of the 'rational consumer'. Governmental responses therefore seek to impose disclosure obligations on sellers of complex goods or products to ensure that consumers have sufficient information upon which to make a decision. Emergent research, based on behavioural economics, challenges traditional ideas and instead focuses on the actual behaviour of consumers. This approach suggests that consumers as a whole do not necessarily benefit from mandatory disclosure because some, if not most, consumers do not pay attention to the disclosed information before they make a decision to purchase. The need for consumer policies to take consumer characteristics and behaviour into account is being increasingly recognised by governments, and most recently in the policy framework suggested by the Australian Productivity Commission

¹ The authors acknowledge the comments and contributions to previous versions of this article by Professor Stephen Corones, Professor, Law Faculty Queensland University of Technology and Mark Burdon, PhD Candidate, Law Faculty, Queensland University of Technology. Any comments and mistakes are however our own.

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for uniform consumer protections laws. The authors will use this policy framework to evaluate current Australian housing information disclosure laws relating to the purchase of residential property. The paper will highlight the policy and legislative assumptions behind the development of those laws and whether those laws are effective in minimising the behavioural biases which cause consumers in the housing market to make errors of judgment. It then will examine the options for strengthening the effectiveness of disclosure regimes in the housing market.

I INTRODUCTION

The effectiveness of consumer protection regulation in Australia was most recently examined by the Productivity Commission in its *Review of Australia's Consumer Policy Framework*.⁵ The terms of reference make it clear that one of the government's key considerations is 'the need for consumer policy to be based on evidence from the operation of consumer product markets, including the behaviour of market participants'.⁶ Similarly the Organisation for Economic Co-operation and Development (OECD) in its Summary Report of the *Roundtable on Economics for Consumer Policy* also highlighted similar concerns noting that current reasons for regulatory intervention in markets do not appear to be grounded on any principled notions of evidence based and ongoing assessment.⁷ Research in the United States⁸ suggests that the traditional approach of empowering consumers, through the provision of increasing amounts of information, without regard to its form or its comprehensibility is detrimental to consumer decision making.⁹ There is growing evidence to suggest that consumers do not take disclosed information into account in their decision making because they do not:

- Read disclosure documentation given to them;
- Understand the documentation if they do read it; and
- Find the information useful.

A study by Miller et al in 2006¹⁰ supports the general findings of the United States' studies in the context of information disclosure in Queensland residential property transactions. The study found that Queensland property experts agreed with the need for disclosure of information to buyers, but doubted whether the benefit to consumers from the disclosure of information outweighed the cost and time involved in the preparation of complex documentation. As such, housing information disclosure laws were

⁵ Productivity Commission, *Review of Australia's Consumer Policy Framework: Final Report* (2008) <<http://www.pc.gov.au/projects/inquiry/consumer/docs/finalreport>> at 17 December 2009.

⁶ Ibid vol 1, vii. Comment about how the terms of reference were established under the Howard Government and it is still not clear how the Rudd Government will move things forward.

⁷ I McAuly, *Roundtable on Economics for Consumer Behaviour: Summary Report* (OECD, 2007).

⁸ C Jolls, and C R Sustain, 'Symposium on Behavioral Realism: The Law of Implicit Bias' (2006) 94 *California Law Review* 969; C Camerer et al, 'Regulation for Conservatives: Behavioural Economics and the Case for 'Asymmetric Paternalism'' (2003) 151 *University of Pennsylvania Law Review* 1211; C R Sustain, 'Informational Regulation and Informational Standing: Akins and Beyond' (1999) 147 *University of Pennsylvania Law Review* 613; S Stern, 'Temporal Dynamics of Disclosure: The Example of Residential Real Estate Conveyancing' [2005] *Utah Law Review* 57.

⁹ Acknowledged by the Productivity Commission, above n 5, vol 2, 33.

¹⁰ R Miller et al, 'Is Mandatory Disclosure an Effective Consumer Protection Mechanism in Australian Real Estate Markets? The Perspective of Queensland Industry Experts' (2006) *Social Change in the 21st Century 2006 Conference Proceedings*.

perceived to have caused an unfavourable impact by increasing the volume of information disclosed which has added to the complexity of compliance.

The calls for change have been such that the OECD has recommended that while mandatory disclosure is important as a consumer protection tool, policy makers should explore its outcome based upon the direct and indirect consequences of consumer behaviour and other factors.¹¹ Biases such as framing and information overload have the potential to result in a consumer making economically detrimental decisions to buy a property that is ultimately unsuitable.

Australia's housing information disclosure laws, as a consumer protection device, are part of a world-wide phenomenon. Governments globally have viewed mandatory information disclosure as a panacea for consumer disadvantage arising from a lack of knowledge about the product being purchased. For example, art 153 of the Treaty of Amsterdam states that 'in order to promote the interests of consumers and to ensure a high level of consumer protection, the Community shall contribute ... to promoting their right to information'.¹² Two thirds of the states in the United States have legislated requiring property condition disclosure in real estate transactions.¹³ Provinces in Canada require property disclosure statements,¹⁴ in the United Kingdom, Home Information Packs are compulsory¹⁵ for anyone marketing a for sale, allowing 'essential information to be made available up front'.¹⁶ Recently the Queensland government has introduced compulsory sustainability declarations upon the sale of a dwelling to:

- increase community awareness of sustainable building features and thereby over time help to improve the sustainability of our community;
- promote the relevance of sustainability features for the value of homes;
- encourage sellers to improve the value of homes by adding sustainable building features; and
- provide valuable information about how the features of an existing home compare to most of the mandatory minimum energy and water efficiency features of a new (or in some cases renovated) home.¹⁷

Although there has been a wide-spread adoption of information disclosure laws for residential property, the rationales for instigation of different laws is by no means uniform and the reasons for Australian government action and the form of this action takes tend not to be based on sound theoretical bases. Consequently, it is difficult in the

¹¹ McAuley, above n 7. Also in its report, the Productivity Commission noted that 'mandatory disclosure requirements have not worked well – sometimes confusing rather than informing consumers': above n 5, vol 1, 11.

¹² See S Haupt, 'An Economic Analysis of Consumer Protection in Contract Law' (2003) 4 *German Law Journal* 1137, 1139.

¹³ G Lefcoe, 'Property Condition Disclosure Forms: How the Real Estate Industry Eased the Transition from *Caveat Emptor* to 'Seller Tell All'' (2004) 39 *Real Property, Probate and Trust Journal* 193, 199.

¹⁴ For example, in Ontario there is the Seller Property Information Statement.

¹⁵ This obligation was imposed on sellers from 1 June 2007.

¹⁶ The Home Information Pack will include energy efficiency, searches and evidence of title, however although the Home Condition Report is not compulsory it will be strongly encouraged by the Government and the real estate industry. See Home Information Pack at <http://www.homeinformationpacks.gov.uk/?aspxerrorpath=/hip_content.aspx> at 17 December 2009.

¹⁷ Explanatory Note, Building and Other Legislation Amendment Bill 2009 (Qld) 9.

case of some disclosure legislation to discern a principled approach by governments to the introduction of mandatory vendor disclosure. In some cases governments have responded to pressure from the electorate or media campaigns professing what the public considers to be fair and just¹⁸ without obtain evidence (through research) that a problem exists.

The application of potentially ineffective measures reflects the historical development of housing information disclosure laws that have been forged in a reactive fashion based on a multitude of ad hoc reasons instead of being guided by a comprehensive audit of existing practices to found the most optimal form of disclosure regulation. While there are legitimate reasons for ensuring buyers are fully aware of the attributes of the property being purchased and the terms of finance being provided, there is growing evidence to suggest that consumers do not take the disclosed information into account in making their decision because they do not read or understand disclosure documentation given to them or do not find it useful.

This article will examine the effectiveness of Australian residential property information laws using the policy evaluation approach suggested by the Productivity Commission in its review. The model suggested by the Commission seeks to implement a more holistic approach by incorporating a consideration of market characteristics, analysis of information failures and a consideration of consumer behaviour. A comparison of the policy response based on the traditional market failure model and the new holistic policy model will be made with the aim of suggesting changes to existing residential property information disclosure laws.

II NEW CONSUMER POLICY FRAMEWORK

As part of the Productivity Commission's *Review of Australia's Consumer Policy Framework*, the Commission recommended an overarching objective for Australian consumer policy:

Australian Governments should adopt a common overarching objective for consumer policy: 'to improve consumer wellbeing by fostering effective competition and enabling the confident participation of consumers in markets in which both consumers and suppliers trade fairly and in good faith'.

To provide more specific guidance to those developing and implementing consumer policy, this overarching objective should be supported by six operational objectives.

The consumer policy framework should efficiently and effectively aim to:

- ensure that consumers are sufficiently well-informed to benefit from, and stimulate effective competition;
- ensure that goods and services are safe and fit for the purposes for which they were sold;
- prevent practices that are unfair or contrary to good faith;

¹⁸ For example, the New South Wales Minister for Fair Trading announced tightening of disclosure laws following a real estate agent's failure to disclose to a prospective buyer that a house was the site of a triple murder (14 October 2004). Available at <<http://www.findlaw.com.au/news/default.asp?task=read&id=21951&site=LE>> at 17 December 2009.

- meet the needs of those who, as consumers, are most vulnerable, or at greatest disadvantage;
- provide accessible and timely redress where consumer detriment has occurred; and
- promote proportionate, risk-based enforcement.¹⁹

To give effect to the Productivity Commission's recommended objective, a new process for evaluating policy instruments was suggested based upon a similar model put forward by the OECD.²⁰ The new process is intended to ensure that a consumer protection problem exists and regulatory intervention is likely to provide a net community benefit.²¹ The model is reproduced below and this paper will refer to the model as the Policy Evaluation Model (PEM).²²

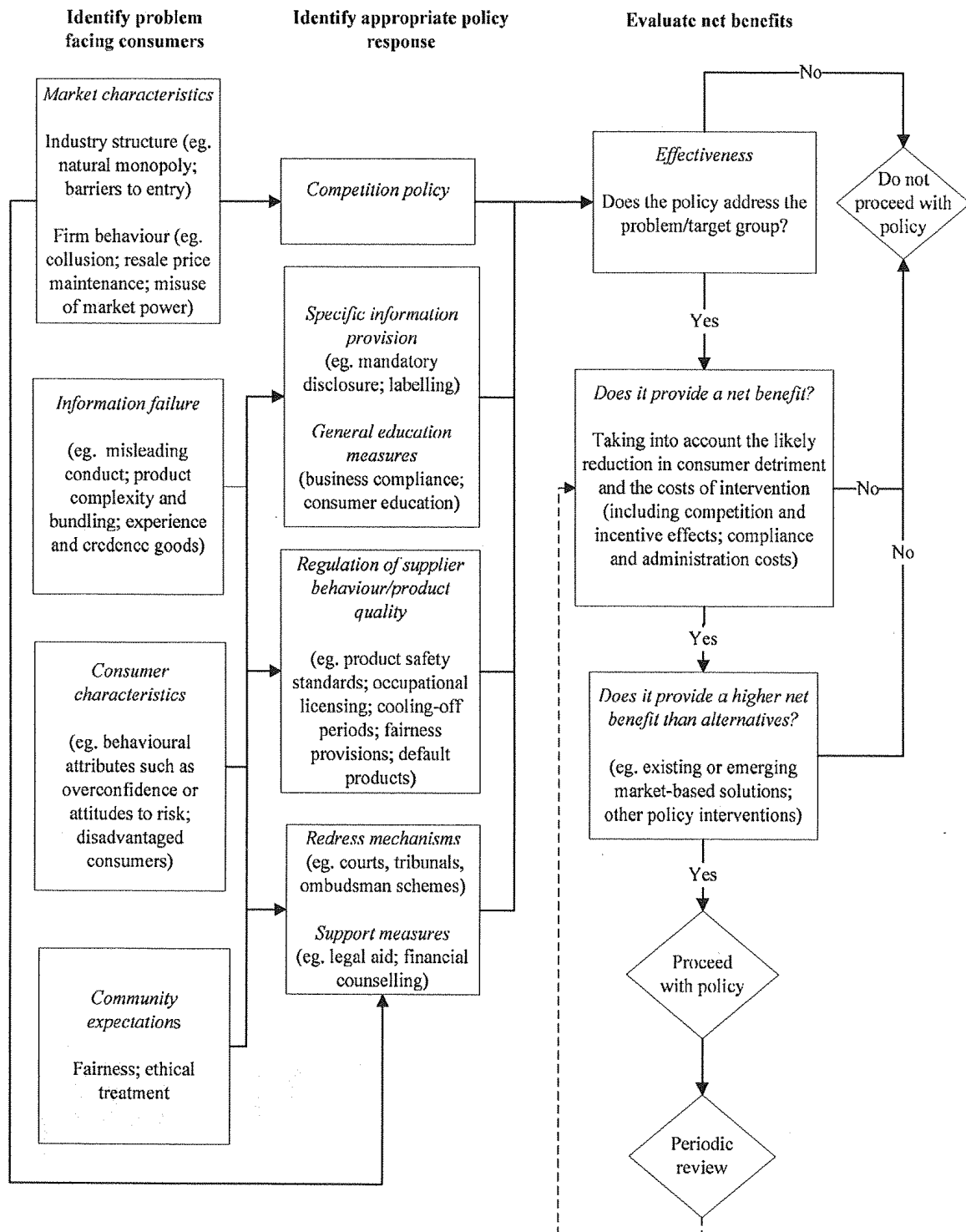
¹⁹ Productivity Commission, above n 5, vol 2, 41-2.

²⁰ McAuley, above n 7.

²¹ Productivity Commission, above n 5, vol 2, 43.

²² Ibid vol 1, 14.

A policy decision-making tree



The PEM suggests a more sophisticated approach to the identification of a potential problem and the appropriate policy response. In contrast to the previously economically driven market failure approach, the PEM invites consideration of the following in identifying the problem:

- (i) What are the characteristics of the market that are affecting competition? Do monopolies operate, is there collusion and resale price maintenance?
- (ii) Is there an information failure? Does the nature of the product mean that consumers are easily misled or cannot obtain information necessary to make a decision?
- (iii) What are the consumer characteristics impacting on consumer decision making?
- (iv) What are community expectations of fairness and ethical treatment in this type of transaction?

The best practice approach advocated by the Productivity Commission at an operational level is:

whenever a new policy initiative is contemplated, or an existing measure reviewed, there should be:

- clear identification of the nature and source of the underlying problem;
- quantification, to the extent reasonably possible, of the associated detriment, or
- prospective detriment, for consumers, or groups of consumers; and
- a comparison of the benefits and costs of all feasible options for dealing with the problem, including relying on market solutions, or employing approaches from outside 'consumer' policy.²³

The remainder of this article reviews and evaluates the effectiveness of current residential property information disclosure laws using the PEM and makes suggestions for changes to those laws that would result in a best practice approach. In accordance with the approach, first the problem will be identified and the associated detriment examined and secondly, the effectiveness of potential responses to the problem will be examined.

III IDENTIFYING THE PROBLEM FACING HOUSING CONSUMERS

A *Common Law Obligations to Disclose*

A common theme underpinning vendor disclosure laws is the clear belief that the general law does not mandate sufficient disclosure nor provide effective remedies for that information failure. This information imbalance arises primarily from the operation of the principle of *caveat emptor qui ignorare non debuit quod jus alienum emi* ('Let a purchaser, who ought not be ignorant of the amount and nature of the interest which he is about to buy, exercise proper caution') which imposed a duty upon a buyer of land to be satisfied as to what he or she is to purchase with no corresponding duty on the seller to disclose information in relation to the property.²⁴ The doctrine recognised that whilst

²³ Productivity Commission, above n 5, 46.

²⁴ For a discussion of the origins of caveat emptor see A M Weinberger, 'Let the Buyer be Well Informed – Doubting the Demise of Caveat Emptor' (1996) 55 *Maryland Law Review* 387; and J B

a vendor could be deemed to have more knowledge of the property he or she owns than a prospective purchaser, the vendor is not deemed to know everything about the property nor does the vendor have any obligation at law to undertake their own searches of the land and disclose the results to the purchaser.²⁵

The doctrine of *caveat emptor* developed in the 16th century when it could be assumed that the vendor and purchaser were of equal bargaining power and that the purchaser did not need special protection.²⁶ Originally *caveat emptor* meant that a vendor was under no obligation to disclose latent or patent defects of a property to a prospective purchaser. A purchaser had no recourse should a property have a defect as the law did not impose upon a vendor a duty of disclosure – mere silence was not and is still not under the common law actionable without more.²⁷ In response to the harshness of a strict application of the doctrine to a buyer, the law developed so as to allow a purchaser to rescind the contract if the vendor had failed to disclose a defect in the title of the property, if that defect was not discoverable by inspection of the property. It followed that to meet the common law obligation a vendor was required to disclose all registered and unregistered interests in the property (leases, easements, mortgages, covenants) but a significant number of other defects which related only to quality but nevertheless affected value (eg zoning, building defects, contamination, heritage) were not required to be disclosed.²⁸

The perceived imbalance of information between a seller and a buyer of real property arguably does require rectification. Prima facie, disclosure of information by a vendor is consistent with considerable literature advocating the advantages of using mandatory information disclosure as a response to a perceived lack of consumer information.²⁹ Stern states in relation to disclosure of defects in real property, ‘the fundamental goals

Pomeranz, ‘The State of Caveat Emptor in Alaska as it Applies to Real Property’ (1996) 13 *Alaska Law Review* 237.

²⁵ *Wilkes v Spooner* [1911] 2 KB 473, 484-5 (Vaughan-Williams LJ); *Zsardonv v Pizer* [1955] VLR 496, 499-500 (Dean J).

²⁶ See Pomeranz, above n 24, 238.

²⁷ See for example *Dormer v Solo Investments Pty Ltd* [1974] 1 NSWLR 428 where a seller remained silent about a proposed pipeline that affected the value of the land. For further discussion refer to D Skapinker, ‘The Impact of the Trade Practices Act on Land Transactions’ (1996) 4 *Australian Property Law Journal* 107; E Webb, ‘Has Caveat Emptor Become Vendor, Lessor and Agent Emptor: Silence, s 52 of the Trade Practices Act 1974 (Cth) and Real Property Transactions’ (1995) 3 *Australian Property Law Journal* 122.

²⁸ *Kadissi v Jankovic* [1987] VR 255, purchaser unsuccessfully sought to rescind contract for purchase of strata title dwelling upon grounds of the existence of serious structural defects. The vendor had made no statements about the structural soundness of the property; *Tsekos v Finance Corporation of Australia Ltd* [1982] 2 NSWLR 347, it was held that negotiations between a seller and the local authority for the resumption of property being sold did not have to be disclosed to a buyer. See also *Carpenter v McGrath* (1996) 40 NSWLR 39 where the lack of formal building approval for a shed was not a defect in title although there was a risk of a notice being issued by the local government to have it demolished.

²⁹ See for example, G K Hadfield, R Howse and M J Trebilcock, ‘Information-Based Principles for Rethinking Consumer Protection Policy’ (1998) 21 *Journal of Consumer Policy* 131; A Schwartz and L Wilde, ‘Intervening in Markets on the Basis of Imperfect Information: A Legal and Economic Analysis’ (1979) 127 *University of Pennsylvania Law Review* 630; H Beales, R Craswell and S Salop, ‘The Efficient Regulation of Consumer Information’ (1981) 24 *Journal of Law & Economics* 491; D Cayne and M J Trebilcock, ‘Market Considerations in the Formulation of Consumer Protection Policy’ (1972) 23 *University of Toronto Law Journal* 396; R Craswell, ‘Passing on the Costs if Legal Rules: Efficiency and Distribution in the Buyer-Seller Relationship’ (1991) 43 *Stanford Law Review* 361.

of defect disclosure are to reduce informational asymmetries, create better matches between buyers and sellers, and increase the fairness of transactions.³⁰

The obvious information imbalance was recognised at the time of introduction of s 52A of the *Conveyancing Act 1919* (NSW), which requires a vendor to attach prescribed documents to a contract of sale of land and imply conditions and warranties, it was stated:

The vendor offering a property for sale has more knowledge that the purchaser about matters affecting the land, such as easements, restrictive covenants and government affectations. It is preferable for the vendor to furnish information about the property rather than to have purchasers competing to obtain sufficient information to be able to exchange contracts in confidence.³¹

It also has to be acknowledged that there is little incentive for a rational vendor of real estate to voluntarily disclose negative aspects or a defect in the property to buyers because this knowledge will impact on the price a buyer is willing to pay.³² Economists argue that high quality sellers will voluntarily disclose information that is costless to verify. This will allow buyers to identify low quality sellers by their silence and discount the price accordingly.³³ There is no evidence to suggest that high or medium quality sellers of real estate voluntarily disclose information about defects to buyers. One reason suggested for this is the lack of consequences for sellers of the failure to disclose under the common law.³⁴ Therefore, the information balance in relation to attributes of the property affecting its value caused by the doctrine of caveat emptor has the potential to disadvantage buyers and lead to:

³⁰ Stern, above n 8, 67.

³¹ New South Wales, *Parliamentary Debates*, Legislative Council, 13 November 1985, 9494 (The Hon J R Hallam (Minister for Agriculture and Fisheries)).

³² Refer to T S Ulen, 'The Growing Pains of Behavioural Law and Economics' (1998) 51 *Vanderbilt Law Review* 1747, 1751.

³³ A Ogus, *Regulation: Legal Form and Economic Theory* (Hart Publishing, 2004).

³⁴ Stern, above n 8, 69 (takes a long time for defects to become discoverable); K A Pancak, T J Miceli and C F Sirmans, 'Residential Disclosure Laws: The Further Demise of Caveat Emptor' (1996) 24 *Real Estate Law Journal* 291, 305 (difficult to prove that the seller knew of a latent defect that failed to disclose).

- (i) Buyers being in danger of exploitation due to a significant information imbalance in favour of the seller. For example, a seller who had knowledge that a gas pipeline was proposed for the property did not have to disclose this to the buyer. This non-disclosure allowed the seller to dispose of the property to an unsuspecting buyer for a higher price than the buyer would have paid if the information was made known.³⁵
- (ii) Buyers being unable to make a proper decision due to the unavailability of information about the quality of the land. This has the potential to result in buyers purchasing 'lemons' due to their inability to judge the quality of the property and the seller being unwilling to provide credible information.³⁶ This is particularly evident in the case of structural defects in a property which could lead to the property being unsuitable for habitation but which a seller is not required to disclose.³⁷

Across Australia, there is general acceptance, both by governments and the judiciary,³⁸ that the information imbalance in the purchase of real property requires the seller to disclose relevant information to the buyer. This perceived need has led to all Australian jurisdictions, except the Northern Territory,³⁹ legislating in respect of seller disclosure in real property transactions.⁴⁰ The disclosure regimes in New South Wales,⁴¹ Victoria,⁴² South Australia,⁴³ Tasmania⁴⁴ and the Australian Capital Territory⁴⁵ attempt to redress this information imbalance by requiring sellers of residential property, (including strata title units) to disclose a significant amount of information related to both the title of the property and its value. In Queensland and Western Australia, only vendors of strata title property are required to make extensive disclosure about the body corporate affairs and property. The effectiveness of these different regimes will be evaluated by reference to the new policy approach advocated by the Productivity Commission.

³⁵ *Dormer v Solo Investments Pty Ltd* [1974] 1 NSWLR 428.

³⁶ Stern, above n 8, 68.

³⁷ See for example *Carpenter v McGrath* (1996) 40 NSWLR 39 where the lack of formal building approval for a shed was not a defect in title although there was a risk of a notice being issued by the local government; *Franich v Swannell* (1993) 10 WAR 459 (no obligation to disclose serious structural defects in the dwelling).

³⁸ *Marinkovic v Pat McGrath Engineering Pty Ltd* [2004] NSWSC 571, [46]. See also *Timanu Pty Ltd v Clurstock Pty Ltd* (1988) 15 NSWLR 338, 339-40 (Kirby P).

³⁹ The Department of Justice of the Northern Territory issued a discussion paper on vendor disclosure in 2006 with a view to amending the *Law of Property Act 2000* (NT) to introduce vendor disclosure (see Northern Territory Government, Justice Department, *Vendor Disclosure*, Discussion Paper, 2006). The Sale of Land (Vendor Disclosure) Bill 2007 (NT) was never introduced to Parliament following a submission from the Property Council and concerns expressed by industry bodies. At the time of writing, an exposure draft of the Sale of Land (Rights and Duties of parties) Bill 2009 (NT) had been released for public comment. The Bill addresses vendor disclosure and cooling off periods.

⁴⁰ See *Civil Law (Sale of Residential Property) Act 2003* (ACT); *Conveyancing Act 1919* (NSW); *Body Corporate and Community Management Act 1997* (Qld); *Land and Business (Sale and Conveyancing) Act 1994* (SA); *Property Agents and Land Transactions Act 2005* (Tas); *Sale of Land Act 1962* (Vic); *Strata Titles Act 1985* (WA).

⁴¹ *Conveyancing Act 1919* (NSW) s 52A.

⁴² *Sale of Land Act 1962* (Vic) s 32.

⁴³ *Land and Business (Sale and Conveyancing) Act 1994* (SA) s 7.

⁴⁴ Part 10 of the *Property Agents and Land Transactions Act 2005* (Tas), entitled 'Land Transactions', contains vendor disclosure requirements in div 2. Part 10 was never proclaimed to commence and in 2009 the Property Agents and Land Transactions Amendment Bill was introduced to the Tasmanian Parliament to amend the uncommenced part. In particular, pt 10 will only apply to residential sales. It is anticipated that pt 10 will be proclaimed in the first half of 2010.

⁴⁵ *Civil Law (Sale of Residential Property) Act 2003* (ACT) s 10.

This analysis demonstrates that the main problem facing consumers of residential property is an information deficit or failure. The problem can be summarised as:

- (i) Sellers know more about the property being purchased;
- (ii) Sellers have no obligation at common law to disclose this information, unless it relates to the title to the property; and
- (iii) Significant information, which may impact on the value of the property cannot be easily discovered by the buyer.⁴⁶

Traditionally, the existence of an information imbalance and the inability of the market to create voluntary obligations of disclosure have given sufficient impetus for government intervention. This intervention has usually been in the form of a requirement for mandatory information disclosure by sellers of residential property to buyers, prior to the buyer signing the contract. Is this a true characterisation of the problem? Will an application of the PEM also result in a case for intervention and would that intervention be in the same form?

B *Are Market Characteristics Responsible for the Problem?*

This may require consideration of a number of issues.⁴⁷ First, is there a market failure? For an economically efficient outcome, markets rely upon parties possessing sufficient information to enable a decision that is in their best interest to be made. To be economically efficient it is not necessary that parties to the transaction possess all information, merely that they possess sufficient information. As stated by Schwartz and Wilde:

The existence of imperfect information is commonly thought to justify market intervention by courts and legislatures because of the predominant belief that an imperfectly informed buyer cannot make utility-maximising purchase choices.⁴⁸

When markets work well in the sense that they are characterised by competitive rivalry, vendors will have an incentive to provide information voluntarily. Arguably, the sale of a residence by its owner may be characterised as workably competitive. It is a one-off transaction and the vendor has no desire to establish a reputation in the market, but the vendor wishes to sell in competition with other vendors with similar properties in the same geographical market. In such a competitive market, there will be an incentive to provide information to the prospective purchaser. However, the incentive to disclose information would not include the disclosure of any negative aspects, instead the disclosure would focus on the favourable aspects of the property. These favourable characteristics, although relevant to a purchaser, would not provide a complete picture to enable the purchaser to make an informed decision about the purchase as has been demonstrated by the erosion of the doctrine of *caveat emptor*.

⁴⁶ This summary arises from the analysis in part 1 of this paper. Further details appear in S Christensen, W D Duncan and A Stickley, 'Evaluating Information Disclosure to Buyers of Real Estate – Useful or Merely Adding to the Confusion and Expense?' (2007) 7 *Queensland University of Technology Law and Justice Journal* 148.

⁴⁷ These three categories are referred to in I Ramsay, *Consumer Protection, Text and Materials* (Wildenfeld and Nicholson, 1989) 34, cited in A B Overby, 'An Institutional Analysis of Consumer Law' (2001) 34 *Vanderbilt Journal of Transitional Law* 1219, 1227.

⁴⁸ Schwartz and Wilde, above n 29, 682.

The market for residential property has characteristics identified by Hadfield et al⁴⁹ as reducing the likelihood that a market based solution will emerge, such as a lack of repeat transactions, the cost to consumers of an unwise decision are potentially catastrophic and the cost of obtaining resolution through the courts is too costly. However, on the positive side the anticompetitive behaviour (resale price maintenance, monopolies, cartels) characteristic of markets for the sale of goods and other products is rare. A more likely scenario is that a seller will engage in anti-consumer behaviour, such as misleading conduct, pressure tactics or harassment to effect a sale. This is due to both the nature of the participants in the market and the nature of the product.

The participants in the real estate market are diverse, ranging from naïve first time buyers and sellers to sophisticated investors and property developers. Unlike other consumer goods, the purchase of a residential property is not a transaction entered into on a recurrent basis nor is it a transaction where purchasers can alter their purchasing decision to punish sellers that do not provide appropriate information. Consequently, there is no incentive for sellers, who may only sell a property once or twice to disclose adverse matters to buyers, who they may never deal with again. The inability of the market to deal with information failures is compounded by the nature of residential property as a product.

First, each property is generally unique. This makes comparison by buyers almost impossible, unless there are a number of similar properties for sale in the same area. For example, where a number of strata title properties are for sale in the same street with similar views and similar features, a seller may be encouraged to provide additional warranties concerning quality or discount the price to ensure a sale. In most other cases, houses will have different features, views and be of differing quality. Consequently, the decision to buy is often based on a personal assessment of the cosmetic attributes and position of the property, rather than what the seller has disclosed.

Secondly, the discovery of adverse impacts on the quality of residential property is often not ascertainable until after a buyer takes possession and, in some cases, not until years later. Latent defects in the structure of buildings on the property,⁵⁰ local government decisions to resume part of the property for infrastructure⁵¹ and flooding levels for the property are some of the matters that can affect the use and value of land and which are not easily ascertainable prior to purchase.

An analysis of the market for residential property suggests that there are no characteristics of the market that will force a vendor to disclose all matters about a property that impact on a buyer's decision to purchase unless required by regulation.

C *What is the Nature of the Information Failure?*

The second key question suggested by the PEM is whether the nature of the product means that consumers are easily misled or cannot obtain information necessary to make a decision? In the case of land, the complex nature of the information and the impact of adverse information on value is also a factor. This complexity creates the potential for a

⁴⁹ Hadfield, Howse and Tebilcock, above n 29, 155-6.

⁵⁰ *Bryan v Maloney* (1995) 182 CLR 609; *Ryan v Hooke* (1987) Q ConvR 54-238.

⁵¹ *Dormer v Solo Investments Pty Ltd* [1974] 1 NSWLR 428; *Tsekos v Finance Corporate of Australia* [1982] 2 NSWLR 347.

buyer of property to be misled by statements or actions of a seller or be unable to ascertain or substantiate important factors that impact on the value of the property. A majority of these factors such as registered leases, easements, mortgages, heritage listing, contamination and local government orders and notices can be readily discovered in most Australian jurisdictions through a search of the appropriate government register. Other significant factors however, such as building defects, proposed resumptions, pest infestations, unregistered or potential interests in land⁵² and flooding are harder to ascertain. In most cases, a seller will be aware or have become aware of factors affecting the property during occupation. At law, a seller is only required to disclose to a buyer the factors affecting the title to the land. This will include:

- (i) the real property description of the property;
- (ii) whether there are any interests affecting the title (and will not be removed prior to settlement) such as leases, easements, mortgages that are registered or unregistered;
- (iii) registered and unregistered statutory encumbrances such as local government sewerage and drainage easements.

This leaves an abundance of information about a property that a seller is not required to disclose. Very few sellers will voluntarily disclose adverse information about the property being sold as this will impact on the price a buyer is willing to pay. The nature of the information not required to be disclosed at law can in some cases impact significantly on the value of the land such as heritage listing which may preclude redevelopment,⁵³ non-compliance with local authority conditions relating to approval for a specific use,⁵⁴ unauthorised alterations to a building under contract,⁵⁵ and even the total absence of building approval.⁵⁶ Does the nature of the information not disclosed by a seller justify intervention or should a buyer be required to ascertain further information. This depends to some extent on whether the information is readily available.

In most Australian jurisdictions restrictions on the use or occupation of land can be ascertained through a search of a relevant body. In Queensland this means a buyer will have to undertake 25 searches to find all information relevant to the use and occupation, and therefore value of the land: The table below provides a summary.⁵⁷

Search/ Relevant Entity	Type of information
Local government Enquiries <ul style="list-style-type: none"> • Rates search • Town planning search • Sewerage and drainage plans 	Rates information, town planning information (zoning, use, future use), position of sewerage and drainage pipes, infrastructure agreements affecting the

⁵² See for example *Dormer v Solo Investments Pty Ltd* [1974] 1 NSWLR 428 where a seller did not have to disclose the potential in the future for a pipeline to be laid across the property requiring an easement, despite the seller having knowledge of this.

⁵³ *Brett v Cumberland Properties Pty Ltd* [1986] VR 107, 110 (Starke J).

⁵⁴ *Re Stranbay Pty Ltd and Catlow Pty Ltd* (1985) Q Conv R 54-180.

⁵⁵ *Mc Innes v Edwards* [1986] VR 161, 165 (Kaye J); Also *Barber v Keech* (1987) 64 LGRA 116, 123 (Kelly SPJ).

⁵⁶ *Carpenter v McGrath* (1996) 40 NSWLR 39, 52-3.

⁵⁷ *Queensland Conveyancing Protocol* (2008) Queensland Law Society <http://www.qls.com.au/content/lwp/wcm/resources/file/ebc03e4640b5593/Q1d%20Conveyancing%20Protocol%20v3%20_10%20September%202008.pdf> at 18 December 2009.

	land, any outstanding IA obligations, any prosecutions for development offences, any plumbing or building show cause or enforcement notices, any outstanding charges against the land
<ul style="list-style-type: none"> Flood search 	Whether the property has flooded and the level of the last flood
<ul style="list-style-type: none"> Building approval search 	Details of building approvals and certificates (including certificate of classification)
<ul style="list-style-type: none"> Health Department search 	Whether the property is registered with the Health Department and any contraventions
<ul style="list-style-type: none"> Swimming pool compliance 	Compliance with swimming pool legislation
<ul style="list-style-type: none"> Heritage search 	Whether property listed on heritage register or any heritage agreements in existence
Vegetation Protection Orders	<p>Details of whether vegetation on the property is protected vegetation or subject to an order</p> <p>(Search of register held by relevant local government)</p>
Land Tax	Whether the property is subject to land tax, if there are arrears and the amount of arrears
Qld Transport <ul style="list-style-type: none"> Roads Port authority (only if on the river) Rail	<p>Current proposals, resumption information for roads, ports and rail</p> <p>(QT will not provide information on proposals for resumptions not currently approved)</p>
Main Roads	Current proposal and future intentions for roads
Queensland Building Services Authority	Details of insurance cover for the property under the <i>Queensland Building Services Authority Act</i>
Environmental Protection Agency	Determine if land is on the Environmental Management Register or Contaminated Land Register*
Vegetation Management (State)	<p>Details of</p> <ul style="list-style-type: none"> Vegetation Clearing Applications Regrowth Vegetation Notifications Vegetation offsets <p>(Search 3 registers in Dept Environment and Resource Management)</p>

Energex/Ergon	<ul style="list-style-type: none"> • If the property is connected under normal tariff conditions; • if the property is connected under guarantee conditions and the amount of the guarantee; • if the property is not connected upon what conditions it may be connected; • whether there are any underground cables running through the property.
Powerlink	Information concerning the Authority's future interest in the property, easements and transmission lines
Court Registers <ul style="list-style-type: none"> • Supreme and District • Bankruptcy register 	<ul style="list-style-type: none"> • If an action has been commenced by or against the seller; • the nature of any action commenced; • copies of all originating summons, interlocutory proceedings, orders, appeals, bills of costs and writs; • the bankruptcy register should provide information concerning name of bankrupt, dates of bankruptcy, and orders
Body Corporate Records Search Only if the property is subject to the <i>Building Units and Group Titles Act 1980</i> or the <i>Body Corporate and Community Management Act 1997</i>	Levy information, by-laws, lot entitlement, insurances, details of management and letting agreement, referee's orders, special levies
Body Corporate Orders (Form 3 BCCM) from Body Corporate Commissioner	Details of Orders made against a particular community title scheme
Qld Fire and Rescue Search This only applies to commercial building and units	Whether a fire safety certificate has been issued for the property, whether the property complies
Bill of Sale Register Only if purchasing chattels, usually commercial property	Details of registered bills of sale
Coastal Management Search	Whether the land is within a coastal management control district or an erosion-prone area and therefore the provisions of the <i>Coastal Protection and Management Act 1995</i> applies
Coastal Protection (Sanctions on construction of jetties)	<ul style="list-style-type: none"> • the date of any sanction issued pursuant to s 86 of the <i>Harbours Act 1955</i> (now part of the <i>Transport Infrastructure Act 1994</i>)

	<ul style="list-style-type: none"> • nature of the works sanctioned
National Heritage Listing	Information on indigenous, natural and historic sites on the register
Mining tenures	Details of mining or petroleum tenures granted
Telco search	Major telecommunication network cables (including Optic Fibre) belonging to Telstra, Optus, UECOMM, AAPT and PowerTel and other providers that pass through the property and information on communications network that may impact on the property

A buyer who undertakes these searches may still not find all relevant information that may impact on a buyer's decision to buy the property. Some adverse factors are not discoverable upon a reasonable inspection of the property, such as the presence of termites and other serious building defects,⁵⁸ crimes that may have occurred on the property⁵⁹ and most significantly proposed actions by government to resume properties⁶⁰ or grant mining leases⁶¹ that cannot be discovered from any search.

D *What are the Consumer Characteristics Impacting on Consumer Decision Making?*

The need to address the general effectiveness of information disclosure through a consumer behaviour model has gained greater acceptance in the last decade.⁶² As part of the PEM, governments are being urged to consider the impact on consumer behaviour on the proposed policy response.

Under a traditional economic model the natural response to market failure arising from a lack of information is to require more information to be given. Under a behavioural model, this is likely to worsen the problem for consumers depending upon the behavioural preferences and cognitive abilities of the consumer. Behavioural economics rejects the assumption that consumers behave rationally and has determined through experiment and empirical observation that consumers depart from predicted rational

⁵⁸ Termites: *Franich v Swannell* (1993) 10 WAR 459; *Walker v Masillamani* [2007] VSC 172; *Eighth SRJ Pty Ltd v Merity* (1997) 7 BPR 15,189, 15,193. Structural defects: *Mitchell v Valherie* [2005] SASC 350; *Kadissi v Jankovic* [1987] VR 255; *Carpenter v McGrath* [1996] 40 NSWLR 39.

⁵⁹ *Hinton v Commissioner for Fair Trading, Office of Fair Trading* [2007] NSW ADTAP 17 (a murder that occurred in the house was not disclosed).

⁶⁰ *Dormer v Solo Investments Pty Ltd* [1974] 1 NSWLR 428; *Tsekos v Finance Corporation of Australia Ltd* [1982] 2 NSWLR 347.

⁶¹ *Borda v Burgess* (2003) 11 BPR 21,203 (failure to disclose a mining lease over the property, held not to be a defect in title because the coal was not being sold).

⁶² Jolls and Sunstein, above n 8; C R Sunstein, 'The Future of Law and Economics: Looking Forward: Behavioural Analysis of Law' (1997) 64 *University of Chicago Law Review* 1175; C Jolls, C R Sunstein and R Thaler, 'A Behavioral Approach to Law and Economics' (1998) 50 *Stanford Law Review* 1471 (individuals realistically display only bounded rationality, bounded willpower, and bounded self-interest); R B Korobkin and T S Ulen, 'Law and Behavioural Science: Removing the Rationality Assumption from Law and Economics' (2000) 88 *California Law Review* 1051.

behaviour due to behavioural biases.⁶³ Despite the lack of empirical evidence in the context of a land transaction, a number of behavioural biases can be identified as having a potential impact on the way a consumer interacts with information about property:⁶⁴

- (i) *Choice/information overload*: economic models suggest that the benefit from extra choice is unfounded. Research in diverse products suggests however, that past a point, when provided with more choice, a consumer either walks away from the market, or chooses randomly. Research shows that consumers who are presented with too much information, legalese or a dense form of words tend not to read the document.⁶⁵ This is especially relevant in the case of real estate transactions where disclosure of a significant amount of information is mandated.
- (ii) *Framing biases*: we are influenced not only by the objective information provided but also by how that information is framed (ie 3% fat or 97% fat free). Each disclosure regime mandates a different form of disclosure and therefore provides a different frame for consideration by consumers.
- (iii) *Anchoring and investment*: individuals anchor on to initial values so that even when that value is uninformative, it influences the final judgement of price, probability or other matters. Where individuals have invested time or money into a transaction, there is a tendency to remain in the transaction despite later prejudicial information that rationally should suggest withdrawal from the transaction. The timing of disclosure is therefore of significant importance with consumers more likely not to enter a transaction than to end a transaction if an adverse matter is disclosed.⁶⁶

In the absence of a vendor disclosure regime, these behavioural biases may have the following impacts:

- (i) The information which can be discovered through inquiries is complex and not presented in a way that is easy for the average buyer to locate or comprehend without legal advice. This may contribute to buyers either not reading the information at all or ignoring it as being too difficult to understand. As can be seen from the Queensland example an unrepresented buyer is unlikely to undertake the 25 searches necessary to locate relevant information. Even if the searches are undertaken the complexity of the information produced means a buyer is unlikely to either read all the information or fully comprehend the consequences.
- (ii) The majority of information is not readily available at the time of contract with buyers usually being advised of adverse impacts, after entry into the contract and payment of a deposit. The cost of searches contributes to the buyer behaviour of only undertaking searches after contract. This is likely to increase the anchoring and investment bias which may lead to a buyer deciding not to terminate because of the money already spent and the uncertainty of recovering the deposit.

These biases suggest that while consumers require a certain amount of information to make an informed decision, any policy response needs to take into account:

⁶³ A number of behavioural biases have been identified in the literature. For a summary refer to McAuley, above n 7, 11-12.

⁶⁴ Stern, above n 8.

⁶⁵ M A Eisenberg, 'Comment: Text Anxiety' (1986) 59 *Southern California Law Review* 305.

⁶⁶ Stern, above n 8.

- (i) The impact too much information or irrelevant information will have upon the decision of a consumer;
- (ii) Whether the way in which the information is presented will impact on the decision of the consumer; and
- (iii) At what point in time should information be made available to the consumer.⁶⁷

Consumer behaviour will also be relevant as to whether information disclosure should be supported by other mechanisms such as cooling off periods, statutory warranties and consumer education.

E *Are there any Community Expectations of Fairness and Ethical Treatment in this Type of Transaction?*

The response of the New South Wales Fair Trading Minister, Reba Meagher to the case involving a failure by a real estate agent to disclose the fact a triple murder occurred in a house, exemplifies the community expectations in the sale of a house:

Buying a home is the largest and most important investment decision most consumers will ever make. Homebuyers have a right to know the details about a property that may affect the value of that property or their decision to buy it.⁶⁸

There is a community expectation that ethically a vendor of real estate should disclose relevant information influential in the decision making process of the purchaser. Mandatory disclosure of information concerning the purchase of a residence may be imposed to achieve this ethical goal – that is, ensure that the purchaser who is naturally in a lesser position than the vendor in respect of knowledge of the property is not taken advantage of.

The reasoning behind this notion is that a lack of a duty upon a vendor to disclose information about the property being sold except so far as the requirements of the principle of *caveat emptor*, may lead to over inflated prices being paid for property. This could lead to a failure of a market. Market efficiencies and increasing the protection of consumers rely upon the consumers being informed. Lack of disclosure in the transaction may lead to a lack of confidence in the property market. For example, the Queensland Government introduced reforms to the business of real estate when two-tiered marketing was taking place in property development. The Explanatory Notes to the Property Agents and Motor Dealers Amendment Bill 2001 (Qld) state:

marketeers have altered their operating tactics to avoid the requirements of the [*Property Agents and Motor Dealers Act 2000* (Qld)]. They have adopted unconscionable practices which continue to result in massive consumer detriment and the erosion of public confidence in the benefits of investing in the Queensland property market.⁶⁹

⁶⁷ These factors have been referred to previously in L Griggs, 'Intervention or Empowerment – Choosing the Consumer Law Weapon' (2007) 15 *Competition and Consumer Law Journal* 111; Christensen, Duncan and Stickley, above n 46.

⁶⁸ Refer to *Gonzales Murder House Leads to New Disclosure Laws* (2004) Find Law <<http://www.findlaw.com.au/news/default.asp?task=read&id=21951&site=LE>> at 17 December 2009.

⁶⁹ Explanatory Notes, Property Agents and Motor Dealers Amendment Bill 2001 (Qld) 1. See also *Jenkins v Kedcorp Pty Ltd* [2002] 1 Qd R 49, 52 for a description of the process of two tier marketing.

Information disclosure in this sense therefore carries with it notions of fairness restoring some symmetry to the transaction.⁷⁰ By requiring a vendor to disclose relevant information to a purchaser it allows the purchaser to make an informed decision about whether to purchase or not – and thereby improves the fairness of the transaction,⁷¹ what is arguably an ethical goal. Providing information to the purchaser ensures that the vendor is not taking deliberate advantage of the purchaser's ignorance and encouraging them to enter into an economically disadvantageous transaction.

IV DETERMINING THE POLICY RESPONSE

The PEM suggests that regulators take into account consumer behaviour in the identification of the problem. The same factors are relevant to a determination of the policy response. McAuley⁷² suggests that intervention in a market by regulators should take account not only of market failure arising from a lack of information failure but also the contribution of consumer biases to the market failure and model the response accordingly. Intervention based on behavioural biases should, however, aim to benefit less rational consumers while not detrimentally affecting rational consumers (for example, in financial and similar markets protection of naive consumers should not distort the decision making of disciplined or well-informed consumers).⁷³ Regulation should also aim to address the problem with a minimum of cost to the community.

The problem as identified in the above analysis is that buyer's of property are disadvantaged under the common law through a lack of readily accessible information about factors impacting on the use and value of the property. The information which can be discovered through inquiries is complex, originates from a variety of sources and is not presented in a way that is easy for the average buyer to comprehend without legal advice. The information is not readily available at the time of contract with buyers usually being advised of adverse impacts after entry into the contract and payment of a deposit.

The traditional policy response to this problem is for regulators to prescribe the mandatory disclosure of information. By disclosing relevant information it is reasoned that purchasers may choose not to buy the property or may negotiate a lower purchase price if they are willing to take on the defects disclosed.⁷⁴ Effective mandatory disclosure should however take into account the complexity of the information and the consumer behavioural biases discussed above. Current vendor disclosure regimes in Australian jurisdictions have to date focused on the content and process.⁷⁵ There has been little research or analysis of the relevance of the information being disclosed, or of the form and presentation of the document if there is one prescribed to discover whether the information is being read and understood by purchasers.

⁷⁰ See also: New South Wales, *Parliamentary Debates*, Legislative Council, 13 November 1985, 9494 (The Hon J R Hallam (Minister for Agriculture and Fisheries)) on the introduction of s 52A of the *Conveyancing Act 1919* (NSW).

⁷¹ Ulen, above n 32, 1751; Stern, above n 8, 67.

⁷² Above n 7, 11-12.

⁷³ Camerer et al, above n 8, 1254. The adoption of asymmetric paternalism as a standard is noted, McAuley, above n 7, 13.

⁷⁴ See Stern, above n 8, 67.

⁷⁵ See for example Tasmania Law Reform Commission and the Justice Department of the Northern Territory.

A *Information Overload*

According to economic theory, disclosure of information is workable if optimal information is achieved. 'Optimal information' is achieved when the marginal benefit derived from the information provided is approximately equal to the marginal cost of providing it.⁷⁶ The administrative and compliance costs associated with information disclosure may exceed the value of the information to the consumer.⁷⁷ If costs of compliance exceed the value or marginal benefit of the information, the government should not intervene.

Behavioural economics recognises however that optimal information may lead to 'information overload', that is, purchasers should not have non-useful information provided in a legal document nor should the information be too detailed or technical. 'Information overload' may result in the purchaser being unable to understand the information being provided. More information is not necessarily better from the purchaser's point of view. While purchasers may derive a measure of reassurance as the level of information provided increases, their ability to make an effective decision may decrease.⁷⁸ Further, inclusion of additional information that may not be as relevant to the transaction may lead to the purchaser ignoring other more important information.⁷⁹

For example, one of the objectives of *The 1999 National Survey of Perceptions of the Franchising Code of Conduct* was to determine the extent to which the Code provides better information to franchisees to enable them to make an informed decision about investing in a franchise. The findings show that only 25.9% of respondent franchisees described the disclosure document as either *important* or *very important*, as compared with 27.7% who described it as *not important*. Only 29.8% of respondents found the disclosure *useful* or *very useful*.⁸⁰ Of the franchisors surveyed, 63.9% claimed that the disclosure requirements had involved additional costs such as legal and/or accounting advice.⁸¹

Research is necessary to determine the relevant information a purchaser will use in making an informed decision about the purchase of residential property. Unless the information provided to the purchaser is relevant to their decision, vendor disclosure is merely adding unnecessary costs to the transaction. It then becomes regulation that achieves no purpose – it is simply imposing additional regulatory burden - red tape with which a vendor must comply and for which there is no perceived benefit.

⁷⁶ Ogus, above n 33, 39.

⁷⁷ Ibid 133.

⁷⁸ Haupt, above n 12, 1142. See also G S Day, 'Assessing the Effects of Information Disclosure Requirements' (1976) 40 *Journal of Marketing* 42, 46 where it refers to studies (J Jacoby, D E Speller and C A Kohn, 'Brand Choice Behavior as a Function of Information Load' (1974) 11 *Journal of Marketing Research* 63) that revealed that the more information provided, poorer purchase decisions were made but the purchasers felt more satisfaction with their decisions. D M Grether, A Schwartz and LL Wilde, 'The Irrelevance of Information Overload: An Analysis of Search and Disclosure' (1986) 59 *South California Law Review* 277, 285 notes that consumers report greater satisfaction with purchases if they perceive that they have more information to base their decision upon even if they did not use that information in their decision process.

⁷⁹ See Camerer et al, above n 8, 1235.

⁸⁰ Australian Franchising Industry, *The 1999 National Survey of Perceptions of the Franchising Code of Conduct* prepared for the Office of Small Business, Canberra by Lawler Davidson Consultants, 37.

⁸¹ Ibid 31.

The key question is therefore, what information does a buyer need to make a reasoned and rational decision to buy a property? ‘The administrative and compliance costs associated with information disclosure should not exceed the value of the information to the consumer’.⁸² Behavioural economics places an emphasis on the use and understanding of the information to optimise the decision making process of the consumer. McAuley states:

some regulation can be ineffective because of poor assessment of its impact, or worse, is costly in terms of imposing high compliance costs on firms. It is possible that behavioural economics can give some guidance as to how regulation can be imposed with a lighter hand. For example, when market failure is addressed in terms of conventional economics, there is often an inclination to require the disclosure of more information. The consequence of a surfeit of information can be information overload, and an opportunity for firms to engage in deliberate ‘confusopoly’.⁸³

The key factor in the purchase of any property is a determination by a buyer of the market price. The market price in legal terms is the price at which a willing vendor is prepared to sell and willing buyer is prepared to buy.⁸⁴ This also assumes that both parties are cognisant of the attributes of the property that impact on price, which include:

- (i) Physical features such as the size of the land, nature and age of the improvements on the land (ie residence, commercial industrial);
- (ii) Factors impacting on the title to the land (encumbrances, title description, statutory changes, judgments or orders, resumptions);
- (iii) Factors impacting on the use of the land (planning and zoning, environmental, heritage, vegetation orders, building approvals, flooding, access);
- (iv) Factors impacting the quality of the improvements (structural defects, building materials, demolition orders).

An analysis of the information currently provided to buyers under the various regimes by Christensen et al reveals 25 different types of information required to be disclosed including titling information, local government planning and building, heritage, contamination, resumptions, energy efficiency, building defects, and flooding.⁸⁵ Despite this extensive list of factors to be disclosed, the authors also identify a number of gaps in the information which in some cases have lead to buyer’s being misled in the purchase of a property. A number of comments can be made about the list of information currently required to be disclosed:

- (i) All of the information a seller is required to disclose has the potential to impact on the price a buyer may be willing to pay the seller.
- (ii) In some cases the information may result in a buyer deciding not to purchase the property for a particular purposed, such as redevelopment.
- (iii) There is significant variation across the jurisdictions ranging from no statutory requirements in Queensland and Western Australia to statutory and contractual

⁸² Ibid 133.

⁸³ Above n 7, 18.

⁸⁴ *Spencer v Commonwealth* (1907) 5 CLR 418, 441.

⁸⁵ Christensen, Duncan and Stickley, above n 46.

- obligations in New South Wales, Victoria, South Australia and the Australian Capital Territory.
- (iv) There is some consistency in the disclosure of matters related to planning and zoning, building approval and prohibitions, government or statutory notices, court judgements or orders, heritage issues, contamination and other environmental issues.
 - (v) Other issues that a reasonable and rational consumer may however consider relevant are dealt with in an *ad hoc* manner:
 - a. building and pest inspections and asbestos reports are only required in the Australian Capital Territory;
 - b. the prospect of flooding is only required in New South Wales; and
 - c. details of structural defects are not required in any jurisdiction.
 - (vi) There is further evidence in the litigation emanating from the jurisdictions with mandatory disclosure that not all information a rational consumer considers relevant is being disclosed.
 - (vii) The information required to be disclosed is in some states very extensive (New South Wales and the Australian Capital Territory) which can lead to disclosure statements being long and complex.

Clearly, there is a need for government regulators to undertake qualitative research and analysis of the information most relevant to consumers of real estate. In keeping with the principle of asymmetric paternalism the resulting list of questions might be posed as follows:

- (i) What inquiries would a rational and reasonable consumer undertake when deciding whether to purchase and at what price?
- (ii) Is there additional information that a rational consumer, if told of the impact of the information on the value of the property require and use in making a decision to purchase?
- (iii) Is there further information that is easy and cost less to provide which would prevent a less than rational consumer from making a bad decision?

To date no Australian research has been undertaken to determine the optimal information required by a consumer to make a rational decision or the additional information required to protect a less than rational consumer from making an unwise decision on a land purchase. Even the most recent analysis by the Tasmanian Law Reform Institute, which led to legislation that imposes mandatory disclosure on sellers of residential property, assumed that disclosure of more information to consumers of real estate was in their best interests.⁸⁶ No evidence of the consumer need for the information or the form in which the information was more likely to be read was produced. The Institute's assessment was based on the literature analysing the doctrine of caveat emptor and its impact on the information imbalance between seller and buyer. The report does not reveal any evidence of consumer disadvantage in Tasmania arising from the information imbalance nor does the report examine if any disadvantages are arising because of the behaviour of consumers in the real estate market. The resulting disclosure regime provides for an increased amount of information to be provided to

⁸⁶ Tasmanian Law Reform Institute, *Vendor Disclosure, Report 5, September 2004* (2004) Faculty of Law University of Tasmania <http://www.law.utas.edu.au/reform/docs/VendDisFinRep200904_A4.pdf> at 21 December 2009.

consumers of real estate, and mirrors substantially the information required in South Australia.

Does it follow that a buyer presented with all of this additional information relevant to the value of the property would use that information in deciding whether to buy and at what price? Should other safeguards, such as statutory warranties and cooling off periods be introduced to safeguard consumers who are overwhelmed by the information provided and are unable as a result to make an informed decision?

B *Framing*

Studies reveal that other factors in addition to the amount of information and detail impact upon a person's decision as to whether they will read the document or not. The appearance of the document and its length also play a role in the decision.⁸⁷ Research into information disclosure reveals that 'the focus on sheer quantity of information also ignores the role of the form and display'.⁸⁸ Therefore, testing of the document is an important step in the process of ensuring the provision of optimal information.

None of the reports undertaken by Australian government bodies into vendor disclosure have tested the documents on their intended audience to determine whether the document is understandable, easy to use and effective. As noted by Howells and Weatherill, 'the policy-maker should be wary of assumptions that (some, perhaps most) consumers are capable of absorbing relevant disclosed information.'⁸⁹

Followers of the emerging behavioural economic theory conclude that consumers do not understand or interpret situations as economists assume.⁹⁰ Therefore, if information must be disclosed in order to protect the purchaser from making the wrong decision it should not be assumed that with that information the purchaser will take the rational course of action or that they will read or even rely upon the information with which the vendor has provided them. Therefore, it cannot be assumed that should the information disclose a defect in the property that the purchaser will have identified the defect or that they have understood the effect of the defect and will attempt to re-negotiate the purchase price or refuse to continue with the purchase.

The first hurdle in designing the disclosure form is to ensure the consumer reads the form. Research in the United States has revealed that most consumers do not read contracts or disclosure forms.⁹¹ For example, research carried out on the adequacy of legal documents reported that 38% of the participant of the study had signed contracts and other legal documents without reading them.⁹²

⁸⁷ M S Wogalter et al, 'On the Adequacy of Legal Documents: Factors that Influence Informed Consent' (1999) 42 *Ergonomics* 593, 610.

⁸⁸ G S Day, 'Assessing the Effects of Information Disclosure Requirements' (1976) 40 *Journal of Marketing* 42, 48.

⁸⁹ G Howells and S Weatherill, *Consumer Protection Law* (Ashgate, 2nd ed, 2005) 25.

⁹⁰ Camerer et al, above n 8, 1230. See McAuley, above n 7, 36 where the author notes that behavioural economics approaches economics as an empirical direction rather than a deductive.

⁹¹ See A M White and C L Mansfield, 'Literacy and Contract' (2002) 13 *Stanford Law & Policy Review* 233, 233 citing T D Rakoff, 'Contracts of Adhesion: An Essay in Reconstruction' (1983) 96 *Harvard Law Review* 1173, 1179.

⁹² Wogalter et al, above n 87, 599.

In the United States, studies reveal that consumers are more likely to read a form that is clear and streamlined. Disclosure structured as a simple checklist with space provided below each item for the seller to describe the nature and extent of any disclosed defects is more likely to be read than one which merely attaches a series of searches or certificates. One study of disclosure revealed that only 3% of buyers found the defect disclosure forms in such a style confusing, while 97% found them easy to understand or understandable.⁹³

Disclosure regimes in Australia adopt differing approaches to the form in which information is given to a buyer. In New South Wales, a seller of residential property is required to disclose a range of matters by attaching a combination of search information and certificates to the proposed contract of sale, supplemented by statutory warranties.⁹⁴ The documents are in the form obtained from each of the relevant authorities. There is no summary of the information disclosed and buyers regularly engage a lawyer to advise them in relation to the purchase. A failure to comply with the disclosure requirements permits a purchaser to rescind the contract by giving written notice within 14 days of making the contract, unless the contract is completed.⁹⁵

The Australian Capital Territory under the *Civil Law (Sale of Residential Property) Act 2003* (ACT) adopts a similar approach to New South Wales. A seller is required to make 'required documents' available to a prospective buyer for inspection at 'all reasonable times' during the offer period and failure to do so is an offence.⁹⁶

Proposed legislation in the Northern Territory will require a vendor to have the required disclosure documents available for inspection and allows for rescission of the contract by written notice if the disclosure documents are not made available.⁹⁷

Victoria and South Australia adopt vendor statements. In Victoria, s 32(1) of the *Sale of Land Act 1962* (Vic) provides for a seller to give a very comprehensive statement of matters affecting the land to the buyer before the buyer signs the contract of sale and include in the contract a statement of those matters.⁹⁸ In addition to the statement prepared by the seller certain specified attachments are required to accompany the statement, being a copy of the certificate of title, evidence of the seller's power of sale where the seller is not the registered owner, evidence of subdivisional approval (where relevant) or evidence of progress toward subdivision (as relevant).⁹⁹ A failure to supply all the necessary information entitles the purchaser to rescind the contract.¹⁰⁰

⁹³ G S Moore and G Smolen, 'Real Estate Disclosure Forms and information Transfer' (2000) 28 *Real Estate Law Journal* 319, 332 (43% easy to understand 55% understandable).

⁹⁴ *Conveyancing Act 1919* (NSW) s 52A(2)(a) and (b).

⁹⁵ *Conveyancing Act 1919* (NSW) s 52A(6); *Conveyancing (Sale of Land) Regulation 2005* (NSW) ss 19, 20.

⁹⁶ *Civil Law (Sale of Residential Property) Act 2003* (ACT) ss 9, 10(1).

⁹⁷ *Sale of Land (Rights and Duties of Parties) Bill 2009* (NT) cls 12, 13.

⁹⁸ There are additional particulars required in the case of a residential sales contract: *Sale of Land Act 1962* (Vic) s 32(1A).

⁹⁹ *Sale of Land Act 1962* (Vic) s 32(3).

¹⁰⁰ *Sale of Land Act 1962* (Vic) s 32(5).

In South Australia, a seller is required to serve a statement upon the buyer in a prescribed form.¹⁰¹ The prescribed form is more detailed than in Victoria essentially requiring the seller to disclose any matter affecting, presently or prospectively, title to, or possession or enjoyment of the land. All particulars required by the prescribed form must be disclosed on the form unless a copy of the document with all details is attached to the statement. The prescribed form is upward of 25 pages of close type with numerous statements in relation to cooling off and other rights together with information concerning encumbrances and defects. If a vendor statement is not provided or does not comply with requirements, a purchaser may apply to court to rescind the contract if the court is satisfied that the purchaser has been prejudiced by the failure.¹⁰²

In 2005, Tasmania passed the *Property Agents and Land Transactions Act 2005* (Tas).¹⁰³ The requirements of vendor disclosure are similar to those of the Australian Capital Territory in that s 186 requires a vendor to have specific documents available while the property is on offer for sale and s 197 implies certain conditions into the contract. If the disclosure requirements are not met a purchaser is entitled to rescind the contract at any time before settlement without penalty by serving a written notice.¹⁰⁴ If a condition of the contract under s 197 is breached a purchaser may rescind the contract or seek damages if the breach causes a loss of 5% or more of the value of the land.¹⁰⁵

There are a number of decisions in New South Wales, Victoria and South Australia that indicate buyers are often misled by both types of vendor disclosure due to the uncertainty of legislation and also the complexity of the disclosure itself. An example of a buyer being misled by uncertain legislation occurred in *Jones v Sherle*¹⁰⁶ where the buyer of a property in New South Wales argued that the seller failed to disclose a declaration under s 55 of the *Public Health Act 1902* (NSW) in relation to a flooding problem which adversely affected the property. Such disclosure, it was argued, was required by virtue of the warranties implied by s 52A(2)(b) of the *Conveyancing Act 1919* (NSW) which at the time of contract warranted that there was no 'declaration under s 55 of the *Public Health Act 1902*'. The Supreme Court refused the claim because at the date of contract the *Public Health Act 1902* had been repealed and replaced by the *Unhealthy Building Land Act 1990* (NSW).

An example of a buyer being misled due to the complexity of the disclosure occurred in *Argy v Blunts & Lane Cove Real Estate Pty Ltd*,¹⁰⁷ where a copy of the local government certificate required to be given was not properly faxed from the real estate agents to the solicitors for the seller, one page having been omitted inadvertently in the fax received. The buyers were misled and entered into the contract prior to discovery of the mistake. Similarly in *Butcher v Lachlan Elder Real Estate*¹⁰⁸ the buyer despite

¹⁰¹ *Land and Business (Sale and Conveyancing) Act 1994* (SA) ss 7, 13A; *Land and Business (Sale and Conveyancing) Regulation 1995* (SA) schs 1, 1A.

¹⁰² *Land and Business (Sale and Conveyancing) Act 1994* (SA) s 15.

¹⁰³ Although the Act commenced upon proclamation on 1 December 2006 (s 2), pt 10 (Land Transactions) containing the provisions relating to vendor disclosure did not commence: Proclamation under the *Property Agents and Land Transactions Act 2005* (SR 2006, No 131), 20 November 2006. At the time of writing, the *Property Agents and Land Transactions Amendment Act (No 2) 2009* (Tas) had been passed, amending pt 10, but have not yet commenced.

¹⁰⁴ *Property Agents and Land Transactions Act 2005* (Tas) s 189.

¹⁰⁵ *Property Agents and Land Transactions Act 2005* (Tas) s 197(2).

¹⁰⁶ (1998) 9 BPR 17,005. See also *Festa Holdings Pty Ltd (in liq) v Adderton* (2004) 12 BPR 22,491.

¹⁰⁷ (1990) 26 FCR 112.

¹⁰⁸ (2004) 218 CLR 592.

receiving a certificate as required by the NSW legislation proceeded to purchase the property despite the inconsistencies in the information provided in the certificate and the information in the sales brochure about the boundaries of the property.

There is evidence in these cases and others¹⁰⁹ that a majority of buyers are unable to interpret and use significant quantities of information leading to later claims for misleading conduct rather than buyer's utilising the termination provisions established by the disclosure regimes. Therefore, if the provision of information is mandated then it is also necessary to mandate the use of plain English and the manner of presentation. If the way the information is communicated is not also regulated it opens up the possibility for complicated legal language to be used to attempt to shroud the meaning of the information from a purchaser.¹¹⁰ It is now well-accepted that legal documents should be in plain English, but the uniqueness of the legal language does provide opportunities for information to be provided in compliance with legislation in such a way that a lay person would have difficulty understanding.

C *Anchoring and Investment*

The timing of the disclosure of the information is also relevant if consumers are to take advantage of the information. Cognitive psychological studies reveal that individuals discount late information and tend to persist in transactions once they have made a commitment. Studies of hypothetical business ventures reveal that consumers tend to continue to invest once they have made initial investments despite later information that counsels for withdrawal.¹¹¹ Education about the sunk costs does not reduce the tendency to persist with a course of action.¹¹² On the basis of the psychological evidence, Stern advocates that early disclosure of information has greater impact on a purchaser's decision making. Disclosure that takes place after committing to a contract has less effect than early disclose because:

People tend to persist in their actions even when the costs increase or the benefits diminish, and they frequently escalate their commitments to failing course of action. Individuals also appear to have greater difficulty processing latecoming information because they over utilize early information - 'or' anchors – in their decision making. These psychological biases towards behavioral compliance, escalating commitment, and

¹⁰⁹ *Franich v Swannell* (1993) 10 WAR 459; *Walker v Masillamani* [2007] VSC 172; *Eighth SRJ Pty Ltd v Merity* (1997) 7 BPR 15,189, 15,193; *Bowler v Hilda Pty Ltd* (1998) 153 ALR 95; *Laudenback v Biedrzycki* (1999) 210 LSJS 424; *Noor Al Houda Islamic College Pty Ltd v Bankstown Airport Ltd* (2005) 215 ALR 625; *Caltex Australia Petroleum Pty Ltd v Charben Haulage Pty Ltd* [2005] FCAFC 271; *Mitchell v Valherie* [2005] SASC 350.

¹¹⁰ See Hadfield, Howse and Trebilcock, above n 29, 143: 'sellers will attempt to minimize disclosure and liability by complying through obfuscation and complex or difficult to decipher (or even receive) statement.'

¹¹¹ H Garland and S Newport, 'Effects of Absolute and Relative Sunk Costs on the Decision to Persist with a Course of Action' (1991) 48 *Organizational Behaviour & Human Decision Processes* 55, 65; H Garland, 'Throwing Good Money After Bad: The Effect of Sunk Costs on the Decision to Escalate Commitment to an Ongoing Project' (1990) 75 *Journal of Applied Psychology* 728, 729-30; D M Boehne and P W Paese, 'Deciding Whether to Complete or Terminate an Unfinished Project: A Strong Test of the Project Completion Hypothesis' (2000) 81 *Organizational Behaviour & Human Decision Processes* 178, 190-1; H Moon, 'Looking Forward and Looking Back: Integrating Completion and Sunk-cost Effects Within an Escalation of Commitment Progress Decision' (2001) 86 *Journal of Applied Psychology* 104, 110-11.

¹¹² H Garland and D E Conlon, 'Too Close to Quit: The Role of Project Completion in Maintaining Commitment' (1998) 28 *Journal of Applied Social Psychology* 2025, 2037-9.

anchoring suggest that latecoming disclosure has a dramatically reduced impact on decision making.¹¹³

Studies have shown that even educated persons aware of the effect of the disclosed information display a ‘deep-rooted response to latecoming information’.¹¹⁴ Therefore, if any defects in relation to the property are disclosed to a purchaser after they have signed a contract to purchase, purchasers are less likely to re-negotiate the purchase price. This is also likely to indicate that cooling off periods are also not likely to be utilised by buyers despite the discovery of adverse information. This behaviour goes against the theory that consumers act rationally and will utilise information disclosed to negotiate a purchase price that takes into account the disclosed defects. It is because of this behaviour that a purchaser will usually still pay more than the value of the property if the defect is disclosed late in the transaction.

As analysed by Griggs¹¹⁵ the disclosure legislation in Australia falls into three categories:

- (i) Disclosure prior to contract signing – Australian Capital Territory and Tasmania;
- (ii) Disclosure around or at the time of contract signing – New South Wales and Victoria; and
- (iii) Disclosure after signing of contract and before settlement – South Australia.¹¹⁶

Griggs argues that the jurisdictions with disclosure after or around the time of contract are not as favourable to buyers, because by this time buyers have invested time and money into the choice of property and are less likely to exercise rights of termination when faced with adverse information.

The likelihood that a buyer may not act on latecoming information is further impacted by the preconditions to rights of termination within the regimes. For example, in New South Wales, a buyer is given a right to terminate the contract provided:

- (i) the right is exercised prior to settlement;
- (ii) the buyer was unaware of the matter at the time of contract;
- (iii) the buyer would not have entered into the contract if they had been aware of the matter; and
- (iv) the buyer has not with knowledge of the inaccuracy of the warranty affirmed the contract.¹¹⁷

¹¹³ Stern, above n 8, 73.

¹¹⁴ Ibid 74.

¹¹⁵ L Griggs, ‘The Content and Timing of Vendor Disclosure in the Sale of Residential Real Estate: Why Both Must be Considered’ (Paper presented at the 2006 Australasian Law Teachers Association, Victoria University Melbourne, 4-7 July 2006). Available at <http://www.alta.edu.au/2006_published_conference_papers.html> at 17 December 2009.

¹¹⁶ Western Australia and Queensland do not have vendor disclosure for residential property. However, both States impose pre-contract disclosure in the sale of strata title property. This would fall within category (i).

¹¹⁷ *Conveyancing (Sale of Land) Regulation 2005* (NSW) cl 19(3). See for example *Azar Building & Construction Services Pty Ltd v Liristis Holdings Pty Ltd (Receivers and Managers appointed)* (2002) 11 BPR 20,523 (valid rescission pursuant to cl 19 where failure of seller to disclose adverse affectation in form of classification of land as having acid and sulphate soils).

The imposition of these restrictions on a buyer's right of termination for the seller's failure to disclose assumes that a buyer, acting properly, will need to verify the information disclosed and verify the accuracy of the warranties given by the seller. If the information is not checked and the matter comes to light after settlement no rights against the seller will exist. This increases the investment cost of the buyer prior to discovering adverse information through confirmatory searches.

V CONCLUSIONS

All Australian jurisdictions, in line with those overseas, have recognised a need to augment the right of a purchaser of residential property to receive information about the property over and above that which the vendor may have been obligated to provide under the general law. This has been due not only to the increase in the array of government regulation of land use and transactions, but also the growing tide of consumer awareness.

Previous regulatory responses by governments to the dilemma of information asymmetry between vendor and purchaser have relied upon traditional economic theory, perceived market imbalance and political and social pressure to justify intervention in the market place. This has resulted in obligations on vendors in most jurisdictions to disclose voluminous and often complex information to buyers in formats that do not ensure buyers will read and understand the information.

The PEM recommended by the Productivity Commission aims to implement a more holistic approach by incorporating a consideration of market characteristics, analysis of information failures and a consideration of consumer behaviour. While adopting the PEM results in the same identification of an information deficit in residential property transactions, a regulator's understanding of the nature and extent of the problem should be enhanced. As demonstrated by this article, the use of the PEM, and therefore a consideration of consumer behaviour, highlights a number of deficiencies in the current disclosure regimes, primarily centring on the failure to ensure information is relevant and presented appropriately.

Studies in the United States have shown the importance of framing information in a clear way using plain English.¹¹⁸ Whether buyers understood the disclosure had a positive impact on the number of unanticipated problems found with the property after settlement.¹¹⁹ Therefore, mandatory disclosure regimes should avoid simply attempting to supply the purchaser with all possible information. A consideration must be had of:

- *When* the information is given to the purchaser;
- Whether the information is *relevant* to the transaction;
- Whether the information is *helpful and useful* and would assist a purchaser in making an informed decision about entering into the transaction;
- Whether the information is in *plain English* and able to be processed and understood by the purchaser; and

¹¹⁸ See Pancak, Miceli and Sirmans, above n 34; L V Zumpano and K H Johnson, 'Real Estate Broker Liability and Property Condition Disclosure' (2003) 31 *Real Estate Law Journal* 285; Moore and Smolen, above n 93.

¹¹⁹ Moore and Smolen, above n 93, 330. Prior to disclosure regimes, 43% of buyers recorded unanticipated problems compared to 8 out of 96 after the passage of mandatory disclosure legislation.

- Whether the *layout* of the document assists the purchaser in reading.

The analysis also highlights the need for some buyers, who either fail to read or understand the disclosure to be given additional protection. Vulnerable consumers can be protected either through statutory warranties in relation to important attributes of the property or a cooling off period. However, the tendency of consumers to remain in transactions once committed may suggest that statutory warranties, which provide rights of termination or compensation is a better choice.

This article demonstrates that whilst there is some consistency in approach by the various governments concerned, the overall picture reveals idiosyncratic requirements and no evidence of any attempt to analyse the effectiveness or the usefulness of the actual disclosure in any case. Clearly, the implementation of an effective disclosure regime for residential property requires evidence based research of consumer behaviour in the context of information disclosure. There is no evidence that any State or Territory government which has adopted a disclosure regime in Australia¹²⁰ has undertaken consumer research to determine what is the optimal level of information from the point of view of balancing the usefulness of the information and its practical effectiveness. This suggests a need for a moratorium upon any additional legislation of this kind, or for that matter any changes, until there is some understanding as to the objectives and effectiveness of vendor disclosure in the residential property market.

¹²⁰ Several studies as discussed have been conducted in the United States.